



Department of Audit 2007 Annual Report

Comptroller of the Treasury

John G. Morgan

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STATE OF TENNESSEE COMPTROLLER OF THE TREASURY

State Capitol Nashville, Tennessee 37243-0260 (615) 741-2501

John G. Morgan Comptroller

December 28, 2007

The Honorable Phil Bredesen, Governor
The Honorable Ron Ramsey, Speaker of the Senate
The Honorable Jimmy Naifeh, Speaker of the House of Representatives and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

The 2007 annual report of the Department of Audit is submitted herewith in accordance with Section 4-3-304 of *Tennessee Code Annotated*.

The Department of Audit conducts audits or ensures that audits are conducted of state, county, and municipal governments; utility districts; internal school funds; and other local government authorities and agencies. Audits are also performed of state grants to nongovernmental organizations and of numerous federal programs for state and local governments.

In submitting this report, I would like to express my appreciation to all those who made possible the results reported, particularly the members of the General Assembly and the staff of this office.

Respectfully submitted,

John G. Morgan Comptroller of the Treasury

JGM/ab





Department of Audit 2007 Annual Report







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Department of Audit

he General Assembly created the Department of Audit in 1937. Authority to audit state and county governmental entities is contained primarily in Section 4-3-304, *Tennessee Code Annotated*. The department is required to:

- perform currently a post-audit of all accounts and financial records of the state government . . . in accordance with generally accepted auditing standards and . . . such procedures as may be established by the comptroller . . .
- make annually, and at such other times as the general assembly shall require, a complete report on the post audit . . .
- certify to the fund balance sheets, operating and other statements, covering the condition of the state's finances, as prepared by the department of finance and administration, or by the state treasurer, before publication of such statements...
- serve as a staff agency to the general assembly, or to any of its committees, in making investigations of any phase of the state's finances...

- make annually an audit of all the records of the several counties of the state . . .
- perform economy and efficiency audits, program results audits and program evaluations...
- require that audits to be performed by the internal audit staffs of grantees or the internal audit staffs of state departments, boards, commissions, institutions, agencies, authorities or other entities of the state shall be coordinated with the office of the comptroller of the treasury and . . . be prepared in accordance with standards established by the comptroller . . .
- require that all persons, corporations or other entities who receive grants from or through this state shall cause a timely audit to be performed, in accordance with auditing standards prescribed by the comptroller . . .

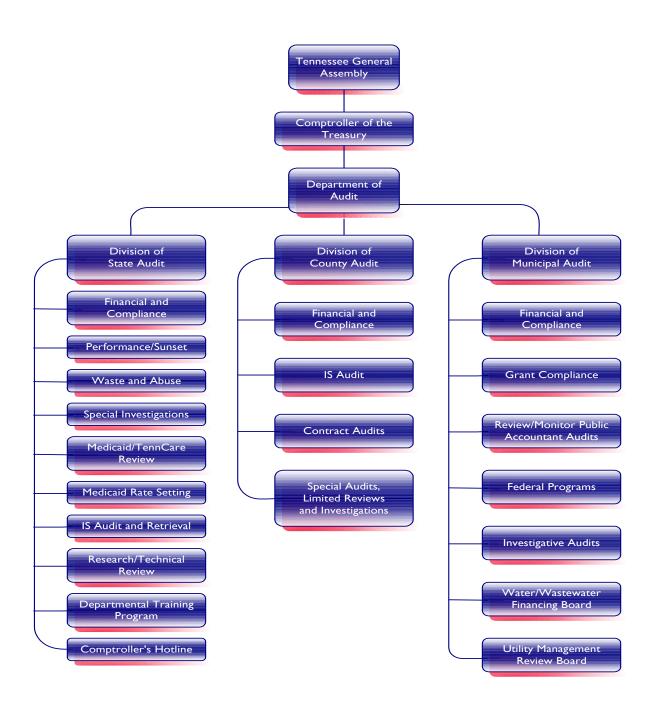
The Department of Audit comprises three divisions—State Audit, County Audit, and Municipal Audit—and employs approximately 300 people. Each division is administered by a director. The three directors are responsible for coordinating the audit function within the department and for addressing concerns and issues in auditing.

The Department of Audit is a post-audit agency. As such, it audits an entity's financial statements; an entity's compliance with applicable statutes, rules, and regulations; and/or its past record of efficiency and effectiveness at the end of a fiscal period.

Because independence is so important in a post-audit agency, the Department of Audit is in the legislative branch of state government. The department is accountable to the General Assembly and provides information to assist the legislature in overseeing the use of public funds and the efficient operation of government.

For additional information on the Department of Audit and Comptroller, go to www.comptroller.state.tn.us.

Department of Audit



Department of Audit

The basic purpose of post-audits is to identify and report past errors and recommend future improvements. Pre-audits, in contrast to post-audits, are performed within an entity by its own employees to prevent errors, detect problems, and suggest improvements. The most important distinction between pre-audits and post-audits is that post-audits are organizationally independent of the audited entity. In this respect, a post-audit agency in government is comparable to an independent public accounting firm in the private or business sector.

Auditing Standards

The Department of Audit performs its audits in accordance with government auditing standards generally accepted in the United States of America as set forth by the Comptroller General of the United States in *Government Auditing Standards* (Yellow Book).

These standards apply to financial and performance audits and attestation engagements. The Yellow Book incorporates auditing standards generally accepted in the United States of America for field work and reporting and attestation standards set forth by the American Institute of Certified Public Accountants.

The Department of Audit conducts its single audit in accordance with the Single Audit Act as amended by the 1996 Single Audit Act amendments and Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations.

Peer Review

To comply with Section 8-4-102, *Tennessee Code Annotated*, the Speakers direct the Department of Audit to undergo a quality assessment review under the auspices of the National State Auditors Association. The most recent review was performed in July 2006 by certified public accountants and other professionals holding executive-level posts in federal and state governments. The purpose of the review was to ensure that the department is meeting its responsibility to perform audit work in accordance with government auditing standards generally accepted in the United States of America.

The report of the peer review for the year ended June 30, 2006, rendered an unqualified opinion on the department's system of quality control. In the opinion of the quality assessment team, "the system of quality control of the State of Tennessee Comptroller of the Treasury, Department of Audit in effect for the period of July 1, 2005, through June 30, 2006, has been suitably designed and was complied with during the period to provide reasonable assurance of conforming with government auditing standards." The next peer review is scheduled for August 2008.

For additional information on the State Auditor's Association, go to www.nasact.gov.



Comptroller of the Treasury Strategic Plan Framework



Mission

To improve the quality of life for all Tennesseans by making government work better

Purpose

To serve the people of Tennessee by:

- Contributing to the protection of the public trust and promoting the public interest
- Enhancing effective public policy decisions at all levels of government
- Fulfilling operational and oversight responsibilities as may be assigned with the highest possible degree of excellence, efficiency, and effectiveness

Goals and Objectives

Assure public resources are used effectively, efficiently, and in compliance with applicable law

- Exercise an oversight role of governmental entities and agencies
- Continue to evaluate the effectiveness and efficiency of resources used by each division through a
 performance-based operation
- Ensure the secure, efficient, and effective use of technology solutions

Accomplish and provide continuous improvement for the statutory and other assigned responsibilities of the Comptroller's Office

- Use cross-divisional teams to address office-wide themes and appropriate strategic objectives
- Continue to advance the Comptroller's Office to a performance-based operation

Provide timely, adequate, and accurate information to decision makers at all government levels

- Maintain a process to develop appropriate information for decision makers
- Maintain a process to provide decision makers with appropriate information concerning policy, resource use, and management
- Encourage cooperation and joint efforts among divisions

Provide a diverse, competent, ethical and professional staff and maintain continual development of such staff

- Adhere to a uniform Code of Ethics Program
- Maintain a succession plan for management
- Maintain a training program for the continual development of all staff
- Seek a healthy and safe work environment
- Review compensation issues within the Comptroller's Office on an annual basis
- Maintain a recruiting and hiring process that promotes diversity

Provide and maintain effective communication with internal and external audiences

- Maintain and improve a program which coordinates timely communications using the best available technology for internal and external communications
- Maintain appropriate historical information
- Inform and educate the citizens of the state, the general assembly, and other government entities about the role of the Comptroller
- Maintain a pro-active presence in professional organizations and associations

Core Values

Honesty and Integrity	Accuracy and Reliability	Accountability
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he Division of State Audit conducts financial and compliance audits, performance audits, and investigations. It also performs special studies to provide the General Assembly, the Governor, and the citizens of Tennessee with objective information about the state's financial condition and the performance of the state's many agencies and programs. This division thus aids the legislature in ensuring that state government is accountable to the citizens of Tennessee. In fulfilling this audit function, the division issued 96 reports during the year ended June 30, 2007; an additional 133 audits and special investigations were in progress at June 30, 2007.

This division includes six sections: financial and compliance, TennCare, performance, waste and abuse, special investigations, and information systems. Highlights of the work each section performed from July 1, 2006, through June 30, 2007, are presented in this chapter. Complete reports are available upon request or on the Internet at www.comptroller.state.tn.us/sa/reports/index.html.

In addition to auditing, the division reviews and comments on exposure drafts from professional organizations and conducts technical research and training. The division also assists the Comptroller in the formulation of state policy and regulations, either directly by consulting with representatives of state agencies or indirectly by submitting comments about proposed policies and procedures.

Financial and Compliance

The financial and compliance section conducts financial and compliance audits of all state departments, agencies, and institutions.

A major endeavor of the financial and compliance section was the Single Audit of the State of Tennessee for the year ended June 30, 2006, conducted in accordance with Office of Management and Budget (OMB) Circular A-133. The Single Audit Report reflected federal awards of over \$10 billion. The results of the audit of compliance indicated that the State of Tennessee complied, in all material respects, with the compliance requirements applicable to each of the state's major federal programs.

However, the results of auditing procedures disclosed instances of noncompliance with compliance requirements applicable to major federal programs that were required to be reported in accordance with OMB Circular A-133.

As a result of testing the state's compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs, costs of \$74,149 were questioned for the year ended June 30, 2006.

The consideration of internal control for the State of Tennessee disclosed numerous reportable conditions; however, none were considered to be material weaknesses in relation to the state's general-purpose financial statements and/or major federal programs.

The Single Audit included an audit of the state's general-purpose financial statements. This audit resulted in an unqualified opinion on the general-purpose financial statements of the State of Tennessee for the year ended June 30, 2006. The audit also determined that the Schedule of Expenditures of Federal Awards was fairly stated, in all material respects, in relation to the general-purpose financial statements taken as a whole.

In addition to the Single Audit Report, separate audit reports were issued on the Department of the Treasury, the Office of the Comptroller of the Treasury, departments administering major federal programs, and units of the government not subject to the control of the centralized accounting system: state universities, community services agencies, the Tennessee State School the Tennessee Local Authority. Development Authority, the Tennessee State Veterans' Homes Board, and the Tennessee Housing Development Agency. The smaller departments and agencies of the government and the community colleges are audited on a biennial cycle.

The separate audits of the departments, agencies, and institutions are not meant to serve as organization-wide audits as described in the Single Audit Act as amended in 1996 and Office of Management and Budget Circular A-133. They do, however, serve as segments of the organization-wide audit of the State of Tennessee; therefore, they include the necessary tests for compliance with applicable laws, regulations, contracts, and grant agreements and the required consideration of the internal control.

The Audit Process

All financial and compliance audits are conducted in accordance with Government Auditing Standards Generally Accepted in the United States of America issued by the United States Comptroller General. The section performs the following general procedures as part of the financial and compliance audit process:

 Reviews the working papers from previous audits and applicable regulations, rules, policies, procedures, laws, and legal opinions.

- Considers the internal control at the entity, including a review of information systems, and determines the nature, timing, and extent of tests to be performed.
- Reviews the original budget and subsequent budget revisions and compares them to actual revenues and expenditures.
- Obtains and analyzes explanations for significant variances.
- Reviews the internal control in the computerized accounting and management information systems.
- Tests to determine the appropriateness of expenditures and the entity's accountability for revenues and cash receipts.
- Tests to substantiate assets, liabilities, and fund balances.
- Reviews federal and state grants to determine the entity's accountability for grant funds and compliance with applicable laws, rules, and regulations.
- Reviews management's representations regarding financial transactions, supporting accounting data, and other disclosure items.
- Evaluates all evidence obtained during the audit process in order to formulate an opinion on the financial transactions and to prepare findings on significant problems.

Results of Audits

During the year ended June 30, 2007, the division published 74 financial and compliance audit reports containing 108 audit findings and issued opinions on 39 sets of financial statements. On June 30, 2007, another 65 audits were in progress. The section released financial and compliance audit reports for the following entities:

Attorney General and Reporter Austin Peay State University

Board of Regents - System Office

CAFR 2006

Department of Children's Services

Department of Children's Services Audit Results

Clean Water State Revolving Fund Comptroller of the Treasury 2006 Comptroller of the Treasury 2007

Department of Correction

Court System

District Public Defenders Conference Dyersbury State Community College

East Tennessee Community Services Agency

East Tennessee State University

Economic and Community Development

Department of Education

Department of Education Audit Results
Endowment for Educational Excellence 2006
Endowment for Educational Excellence 2007
Department of Finance and Administration

Hamilton County Community Services Agency

Department of Health

Department of Health Audit Results

Human Rights Commission
Department of Human Services

Knox County Community Services Agency

Department of Labor and Workforce Development

Local Government Group Insurance Fund

Medicare Supplement Insurance Fund

Department of Mental Health and Developmental

Disabilities

Mid-Cumberland Community Services Agency

Middle Tennessee State University

Military Department

Motlow State Community College

Nashville State Technical Community College

Northeast Community Services Agency

Northeast State Technical Community College

Northwest Community Services Agency

Pellissippi State Technical Community College

Post-Conviction Defender Commission

Department of Revenue

Roane State Community College

Roane State Community College Foundation

Single Audit 2006

South Central Community Services Agency Southeast Community Services Agency 2006 Southeast Community Services Agency 2007 Southwest Community Services Agency 2006 Southwest Community Services Agency 2007 Southwest Tennessee Community College

Teacher Group Insurance Fund

TennCare

Tennessee Arts Commission

Tennessee Education Lottery Corporation

Tennessee Residence Foundation
Tennessee Sports Hall of Fame
Tennessee State University 2006
Tennessee State University 2007

Tennessee Consolidated Retirement System

Tennessee Corrections Institute

Tennessee Housing Development Agency Tennessee Local Development Authority Tennessee State School Bond Authority

Department of Transportation

Department of Transportation Audit Results

Department of the Treasury U.T. Radio Station (WUOT) University of Memphis University of Tennessee

Upper Cumberland Community Services Agency 2006 Upper Cumberland Community Services Agency 2007

Veterans Home Board

Walters State Community College

Recurring Findings: Financial and Compliance Audits	No.
Noncompliance with state or federal laws or regulations	24
Inadequate controls over contracts, including subrecipients	14
Inadequate controls over expenditures	11
Potential loss of revenues	10
Payroll and personnel issues	8
Inadequate controls over accounting or management information systems	6
Noncompliance with state purchasing policies and procedures	6
Inadequate controls over equipment or vehicles	6
Inadequate controls over residents' or children's trust funds	5
Bank reconciliations not properly prepared	4
Inadequate control over financial reporting	4
Lack of proper risk assessments	3
Inadequate controls over inventory	2

Performance

A performance audit is an independent examination of the extent to which agencies and departments of state government are faithfully carrying out their programs. The audit reports assist the General Assembly and agency management by

- assessing the extent to which state agencies have fulfilled their statutory mandate and the efficiency and effectiveness of management's organization and use of resources,
- developing recommendations for management or legislative action that might improve the efficiency and effectiveness of the agency's operations, and

 providing pertinent program and financial data about the agencies.

Most of the performance audit section's workload is performance auditing directed by the Tennessee Governmental Entity Review Law, commonly known as the Sunset Law (Section 4-29-101 et seq., *Tennessee Code Annotated*). This law requires that each agency, board, commission, or other entity be reviewed at least once every eight years by the legislative Joint Government Operations Committee to determine whether that entity should be continued, restructured, or terminated.

Audit staff focus their efforts on the audits of major entities. In the year ended June 30, 2007, the performance audit section released 10 audit reports covering 12 entities; 18 projects were in process at year-end. The Government Operations Committees held 13 public hearings on 45 entities in the year ended June 30, 2007. At these hearings, performance audit staff presented audit reports covering 20 entities. Another 23 entities submitted written responses to staff-prepared questions based on the entities' statutory authority and responsibility. Two entities updated committee members on their activities, including actions taken in response to audits presented in earlier years.

Audit Process

Performance audits are conducted in accordance with Government Auditing Standards issued by the United States Comptroller General. Audits progress through six phases: planning, detailed audit field work, report writing, comments from agency management, publication of the final report, and presentation of the final report at a legislative hearing. Performance auditing includes the following activities:

- Review of relevant state and federal laws, court cases, Attorney General's opinions, executive orders, rules, and regulations.
- Review of the agency's procedures, plans, and policies.
- Examination of the agency's records, files, and correspondence.
- Interviews with staff of the audited agency and related agencies.
- Observation of the agency's operations and activities.

- Analysis of the agency's revenue and expenditure data.
- Analysis of the agency's program data, performance measures, and reported results.
- Review of comparative data from other states.
- Surveys of individuals, agencies, and organizations served or affected by the agency.
- Tests for compliance with significant legal and administrative requirements.
- Evaluation of the extent to which the agency achieved desired results at the lowest reasonable cost.
- Recommendations of possible alternatives for legislative or administrative action that may result in more efficient and effective accomplishment of the agency's legislative mandate.

The performance audit section released 10 audit reports covering the following 12 entities:

Board for Licensing Contractors
Commission on Children and Youth
Department of Children's Services,
Division of Child Protective Services
Department of Education
Department of Human Services
Department of Mental Health and
Developmental Disabilities
Department of Transportation
Home Improvement Commission
Human Rights Commission
State Board of Education
Tennessee Commission on Aging and Disability

University of Tennessee Board of Trustees

Recurring Findings: Performance Audits	No.
Inadequate monitoring systems	8
Inadequate strategic plans, policies, and goals	5
Policy and statute noncompliance	5
Review and revision needed for policies, statute, or processes	5
Timeliness	4
Conflict-of-interest policies and disclosures	2
Board and commission membership	2
Title VI	2
Data verification and reliability	2
Under-use of available resources	2
Security of files	1
Duplication of services	1
Inconsistent performance	1
Information systems	1
Lack of statewide services	1

Waste and Abuse

The waste and abuse section is focused on looking at waste and abuse or the potential for waste and abuse. According to Government Auditing Standards (the Yellow Book), "Abuse is distinct from illegal acts and other noncompliance. When abuse occurs, no law, regulation, contract provision or grant agreement is violated. Rather the conduct of a government program falls far short of societal expectations for prudent behavior." The section produces special reports highlighting areas where state agencies have not acted in the best interest of the state. The special reports are generally briefer than our audit reports. Members of this section look at issues with only one or two objectives instead of the more comprehensive scope addressed in traditional performance audits, but often cover the same issue in numerous state agencies. Topics for the waste and abuse section projects may be originated by any source, including the Comptroller of the Treasury, the Director of State Audit, management and staff of any division of the Comptroller's Office, a legislator, someone in another part of state government, or someone outside of state government. Seventeen audits were in progress on June 30, 2007.

TennCare

The TennCare section of the Division of State Audit, under an agreement with the Department of Finance and Administration, performs certain audit and rate-setting functions for the state's TennCare program.

A staff of 20 professional auditors performs the following functions:

- Reimbursable rate computation and examinations for nursing homes and Intermediate Care Mental Retardation facilities that participate in the Medicaid Program.
- Examinations of TennCare Managed Care Contractors (MCCs) that contract with the state to provide medical services under the program. The examinations are performed jointly with, and released under, the Department of Commerce and Insurance.

- Agreed-upon procedures engagement performed to compute the Certified Public Expenditures (CPE) for public hospitals. CPE is defined as unreimbursed TennCare costs. The TennCare waiver provides for additional federal funding depending on the level of CPE in public hospitals.
- Computing of reimbursement settlements and prospective rates for Federally Qualified Health Centers and Rural Health Clinics as required by the Benefits Improvement and Protection Act of 2000.
- Provide financial and budgeting support to the Bureau from nursing home paid claims extracts.
- Cost settlements for state-operated Development Centers that provide services to mentally retarded recipients.
- Clinical monitoring of the state's Mental Retardation Waiver project.

Examinations of Nursing Facilities

In fiscal year ended June 30, 2007, the TennCare section completed eight examinations of the following Nursing Facilities and Intermediate Care/Mental Retardation Facilities.

Bells Nursing Home
Comcare
Jefferson City Health and Rehabilitation Center
Pine Meadows Healthcare and Rehabilitation Center
St. Francis Nursing Home
The Margie and Thomas Winfrey Center
Wayne County Nursing Home
Weakley County Nursing Home

The examinations reported findings such as

- Nonallowable expenses
- Inaccurate accumulation of resident days
- Residents inappropriately charged for covered services
- Charges on cost report not supported by financial records

Examinations of TennCare MCOs and BHOs

In fiscal year ended June 30, 2007, the TennCare section assisted the Department of Commerce and Insurance in performing three examinations of MCCs. Examples of significant findings reported included

- Deficiencies in claims processing system
- Deficiencies in provider contract language
- Failure to comply with prompt pay requirements
- Failure to return interest earned and subrogation amounts to the state in a timely manner
- Noncompliance with statutory accounting principles

Special Projects – Grier Consent Decree

The state, legislature, or federal government often requests that the Division of State Audit work on special TennCare projects. One such project is currently in progress.

The state, under a consent decree with the federal court, has agreed to comply with certain requirements with respect to TennCare enrollee grievances and appeals. The TennCare managed care contractors and their providers are also subject to the consent decree, so it has widespread implications. The agreement, commonly referred to as the "Grier Consent Decree," became fully effective on November 1, 2000.

The Grier Consent Decree requires the state to enter into an agreement with the Comptroller's Office to monitor all aspects of compliance with the order and to report quarterly. Quarterly reports through December 31, 2006, have been completed, and the reports for the quarters ending March 31, 2007, and June 30, 2007, are in progress.

Special Investigations

Authority to conduct special investigations is provided in part by Sections 8-4-201 through 8-4-208, *Tennessee Code Annotated*. The special investigations section gathers information and evidence resulting in prosecutions and recovery of funds and coordinates the efforts of other agencies involved in the investigation. The investigators assist local district attorneys general, Tennessee's Office of the Attorney General, the Office of the United States Attorney General, and the Tennessee Bureau of Investigation.

Investigative reviews are initiated as a result of information discovered during audits by the Department of Audit and through information from individuals or other departments and agencies. The matters investigated during the fiscal year

ended June 30, 2007, ranged from embezzlement of public funds to abuse of public resources. Twenty investigations were in progress at June 30, 2007. Investigations were completed on matters at the state level as well as matters at the local level. Investigators often found that losses were incurred as a result of weak internal control or ineffective management.

Ongoing investigative reviews resulted in

- the receipt of the final \$100,000 of a judgment for \$250,000,
- one employee who retired in lieu of termination, and
- two terminations during fiscal year 2007.

Information Systems

The information systems (IS) section provides three basic services: data retrieval, IS systems review, and computer forensic analysis.

The data retrieval staff provide information for audit field work. They write computer programs to provide information from the state's centralized accounting system, individual agency service delivery systems, and college and university transaction files.

The IS review staff are responsible for obtaining and documenting an understanding of the internal control structure in the computerized accounting and management information systems of entities undergoing financial and compliance audits.

The IS section provides services in the area of computer forensic analysis. Evidence of fraud and abuse may be found on subjects' computers, and the IS section works in support of the special investigations section to acquire, identify, and analyze this evidence. The section utilizes specialized software and hardware to recover evidence of official misconduct by state employees and in support of civil or criminal action against persons or entities engaging in illegal activities resulting in damages to the state.



he Department of Audit, through the Division of County Audit, is responsible for the annual audits of all 95 counties in the state. The division may conduct the audit of a county or accept an audit prepared by a certified public accountant provided the audit meets minimum standards for county audits established by the Comptroller of the Treasury. However, the Division of County Audit is required to prepare an audit in each county at least once every five years or to participate with, or monitor the audit with, the certified public accountant.

Financial and Compliance

The division presently conducts audits in 89 counties. These audits are assigned to teams that audit the various offices and/or departments and entities of county government. The audit staff is divided into four geographical areas: East, Mideast, Middle, and West. Each area is under the supervision of an audit manager who is responsible for audit planning and supervision.

The Audit Process

The Division of County Audit performs the following general procedures as part of the financial and compliance audit process:

- Evaluates the entity's existing internal controls in the appropriate areas of operation.
- Confirms the accountability for receipts by examining, for example, tax rolls, state and federal revenue data, and letters of inquiry.
- Determines the appropriateness of disbursements by examining budget authorization, paid invoice files, purchasing files, payroll records, and other financial records.
- Determines the authorization for transactions by reviewing the minutes of meetings of county commissions, school boards, highway commissions, and various committees such as budget and finance, and purchasing.
- Determines compliance with federal regulations and state and local laws.
- Obtains management's representations with respect to the financial statements, as well as the supporting accounting data, and other items of disclosure.

- Evaluates financial statement presentation to determine conformity with generally accepted accounting principles.
- Evaluates the validity of all evidence obtained throughout the audit process to formulate an opinion on the financial statements.

Scope of Activity Post-Audit of County Governments

The Division of County Audit conducted audits in 89 of the state's 95 counties during the 2006-07 audit year. A minimum of ten offices or departments in each county was audited:

- 1. County Trustee
- 2. County Mayor
- 3. Department of Education
- 4. Department of Highways
- 5. County Clerk
- 6. Circuit Court Clerk
- 7. General Sessions Court Clerk
- 8. Chancery Court Clerk and Master
- 9. Register
- 10. Sheriff

The audits of all offices were for the year ended June 30, 2006. The audit field work in each county is conducted by an audit team. The size of the team is determined by the complexity of the assignment. Approximately ten weeks of field work are required, including audit review and supervision by an auditor 4 and/or audit manager. The draft audit reports are reviewed in the Nashville office, printed and released. The division also prepares audits of two special school districts and performs special audits and reviews as requested or as deemed necessary.

Results of Audits

Financial and Compliance Audits

Audits of financial transactions for the year ended June 30, 2006, conducted by the Division of County Audit disclosed cash shortages in the following offices or funds:

Anderson County Trustee's Office	\$ 30,126
2. Anderson County Clerk's Office	1,782
Campbell County Clerk's Office	3,969
4. Cumberland County Ambulance Service	2,717
5. Decatur County School Department	13,824
6. Dickson County Circuit Court Clerk's Office	1,350
7. Franklin County Juvenile Court Clerk's Office	24,752
8. Gibson County Health Department	6,991
9. Hardeman County Solid Waste Department	20,903
10. Hickman County Emergency Communications District (E-911)	11,773
11. Henry County Sheriff's Office	162,657
12. Morgan county Clerk's Office	14,756
13. Robertson County Clerk's Office	1,902
14. Rutherford County School Department	3,031
15. Sumner County School Department	7,122
16. Tipton County School Department	820
17. Unicoi County General Sessions Court Clerk's Office	21,431
18. Union County Court Clerk's Office	5,903
19. Van Buren County Mayor's Office	7,428
20. White County Sheriff's Office	1,108
21. Williamson County Recreational Center	<u>45,037</u>
Total Cash Shortages	\$389.382

The audits conducted by this division disclosed fund deficits of \$91,546,544 in 57 governmental fund accounts in 43 counties. Audits also reflected net asset deficits totaling \$14,304,662 in 10 enterprise funds and 3 internal service fund accounts in 11 counties.

The division's examination of offices and departments in 89 counties resulted in several recurring audit findings summarized on the next page.

Recurring Findings	No.
Government-wide financial statements were not prepared.	41
A system of central accounting, budgeting, and/or purchasing was not in use, frequently resulting in inefficient and uneconomical operations of various county offices and departments.	52
Fund expenditures exceeded appropriations approved by the local governing body.	20
Purchasing procedures were not in accordance with controlling statutes.	37
Clerks of court failed to prepare and/or reconcile a trial balance of execution docket balances with cash journal accounts.	12
Drug control funds were not administered in compliance with statutory provisions.	11
Funds were not deposited within three days of receipt, as required by state law.	34
Depositories for county funds were not required to place securities in escrow in sufficient amounts to adequately protect funds on deposit, as required by state law.	8
Loans, notes, or lease-purchase agreements were not approved by the County Commission and/or director of Local Finance.	24
Fees and commissions earned by the county clerk, clerks of court, and register were not remitted to the county in compliance with controlling statutes.	12
nventory records of assets owned by the county were not maintained, as required by generally accepted accounting principles.	27
Deficiencies occurred in accounting/recordkeeping.	84
An internal control weakness resulted due to the inadequate segregation of duties for accounting personnel.	78
Purchase orders were not used or were not issued properly in the purchasing process.	40

Contract Audits

In six counties, certified public accountants perform financial and compliance audits. The division monitors these audits in accordance with a four-year monitoring plan which includes a review of working papers prepared by certified public accountants.

The division also approves the contracts of certified public accountants and reviews their audit reports and working papers. The objective of this review is to ensure that in addition to the standards prescribed by the American Institute of Certified Public Accountants and Government Auditing Standards issued by the United States Comptroller General, certain standards prescribed by the Comptroller of the Treasury have been followed.

Scope of Activity Monitoring and Review of Contract Audits

The division will monitor audits of six county governments during the next four years. The audit of Hamilton County was monitored for the year ended June 30, 2006, and the audits of Washington and McMinn Counties will be monitored for the year ended June 30, 2007.

The division reviewed 279 audit reports for the year ended June 30, 2006, submitted by certified public accountants for audits of county governments, authorities, boards, commissions, agencies, and special school districts. The division anticipates it will review 287 such reports for the year ended June 30, 2007.

Information System Reviews

Most county government offices and departments in Tennessee have automated all or a portion of their daily operations. The information system (IS) review section is responsible for conducting reviews of those computer-based accounting and information systems to determine whether an entity's existing procedures and controls provide adequate assurance of data accuracy and financial and operating statement reliability. An assistant director supervises this section's IS audit manager and seven IS auditors, who are assigned to different areas of the state.

An IS systems review consists of a review of the general and application controls of a county's computer hardware and computerized accounting and information systems. Findings resulting from an IS review are discussed with the appropriate officials and presented in a report on the internal controls regarding computer operations in the county. The IS findings also may be included in the county's annual financial report.

Scope of Activity Information System Reviews

IS systems reviews were conducted in 37 counties and two special school districts during the year ended June 30, 2007. The division anticipates that controls over information will be examined in 89 counties and two special school districts during the year ending June 30, 2008.

Other Services

Technical Assistance

In addition to the basic post-audit function and the monitoring and review of audits by certified public accountants, the division provides other services. These services include providing assistance, upon request, to counties in resolving current problems with financial administration, as well as answering questions on various local governmental matters.

Reviews of Funds Administered by District Attorneys General

During 2007, the division conducted reviews of District Attorney General Funds, Judicial District Drug Task Force Funds, and other funds the district attorneys general administer in the state's 31 judicial districts. Each review covered the period July 1, 2005, through June 30, 2006. The scope of each review was limited to the transactions of the individual funds and did not include the overall operation of the district attorneys' offices.

Reviews of County Correctional Incentive Program (CCIP)

Tennessee Code Annotated, Title 41, Chapter 8, referred to as the County Correctional Incentive Act, provides counties financial incentives to house nondangerous felony offenders at local correctional facilities. The purpose of the program is to mutually benefit state and county governments by helping to alleviate overcrowding in state correctional facilities and reduce high operating costs, and to assist counties in upgrading local correctional facilities and programs. Counties participating in the program

may be reimbursed at either a minimum statutory daily rate or a rate based on a county's "reasonable allowable cost" to house convicted felons.

The Division of County Audit conducts reviews of counties participating in the County Correctional Incentive Program. In performing the reviews, the division tests the county's financial records and other supporting records pertaining to the Final Cost Settlement Reports. Test work is also performed on the Correction Facility Summary Reports and State Prisoner Reports. Reviews were conducted in 25 detention facilities during the 2006-07 audit year. As a result of the reviews, it was determined that the state had overpaid \$985,710 for 12 facilities and underpaid \$141,567 for three facilities.

The reviews of ten facilities resulted in no over or underpayments. The record-keeping system for two facilities with noted overpayments did not allow us to make a reasonable determination of over or underpayments, and a final cost settlement for these facilities was at the discretion of the Department of Correction. Subsequent monthly claims filed by the affected counties have been or are being adjusted to reflect the underpayments or overpayments.



Municipal Audit

he Division of Municipal Audit ensures that annual audits, required by state statute, are performed for all Tennessee municipalities, public school activity and no centralized cafeteria funds, utility districts, housing authorities, charter schools, and certain nonprofit agencies receiving grants from the State of Tennessee. Also, as required by state statute, the division ensures that an agreed-upon procedures audit is performed for certain daycare providers receiving subsidy payments through the State of Tennessee. In addition, the division investigates allegations of misconduct, fraud, and waste in these entities.

Audit Review Process

Local governmental units (other than counties) and nonprofit agencies contract with independent certified public accountants to perform annual audits of Tennessee's 344 municipalities, 104 city-related entities, 70 quasi governmental entities, 51 quasi nonprofit entities, 182 utility districts, 163 public school activity and no centralized cafeteria funds, 10 charter schools, 85 housing authorities, 3 housing authority related entities, 51 day care centers, and 204 nonprofit agencies. The entities use standard contracts, prepared by the Comptroller of the Treasury, that must be approved by the Comptroller's designee in the Division of Municipal Audit before audit work begins. These audits must be performed in accordance with generally accepted government auditing standards or agreed-upon procedures certain other minimum requirements prescribed by the Comptroller of the Treasury. In addition, the auditor must comply with certain other federal and state provisions.

The Division of Municipal Audit reviews each audit report to verify that it adheres to applicable reporting requirements. If a local governmental unit or nonprofit agency fails or refuses to have an audit, the Comptroller may direct the Division of Municipal Audit, or may appoint a certified public accountant, to perform the audit. The division evaluates the audit working papers of certified public accounting firms that audit local

governmental and nonprofit entities. If the firm's audit working papers are deemed substandard, the Comptroller of the Treasury takes appropriate action, which might include referral to the State Board of Accountancy. The division is responsible for tracking 2,221 nonprofit organizations that have received grants from the State of Tennessee; some of these organizations are required to have an audit of their entire organization. These audits are conducted by certified public accounting firms which contract with the division.

Sections 68-221-1010 and 7-82-401g(1), Tennessee Code Annotated, require the Comptroller to refer financially distressed municipal wastewater and public utility districts to the state's Water/Wastewater Financing Board or the Utility Management Review Board. After reviewing the audit reports, the Division of Municipal Audit refers financially distressed facilities to the appropriate board. The board then reviews the current financial condition of the facility and its proposed plan for eliminating its financially distressed condition. If the board finds the facility's plan unacceptable, the board will recommend an alternate course of action.

Municipal Audit

During the year ended June 30, 2007, 24 municipal wastewater facilities were referred to the Water/Wastewater Financing Board, and 12 utility districts were referred to the Utility Management Review Board. As a result, several utility districts and municipal water and/or sewer systems are now operating or are on their way to operating on a financially sound basis.

Investigative Audits

The division investigates allegations of misconduct, fraud, and waste in specified local governments and other publicly funded entities. Investigative audits are performed as a result of allegations received through the Department of Audit's toll-free hotline, routine audit reviews, information received from certified accountants, other state agencies, concerned citizens and/or officials, and requests received from local district attorney generals, the State Attorney General's Office, the FBI, and other prosecutorial and law enforcement agencies. Upon completion of each examination, the Comptroller issues a report or letter presenting documented occurrences of improper activity and recommending corrective action. The report is forwarded to the State Attorney General and the local district attorney general for any legal action deemed necessary.

The division also conducts investigative audits that include a thorough review of the internal control structures and compliance with applicable laws. Municipalities are required by statute to maintain their records, at a minimum level, in accordance with the *Internal Control and Compliance Manual for Tennessee Municipalities*, prescribed by the Comptroller of the Treasury. Utility districts are required by state statute to follow the *Uniform Accounting Manual for Tennessee Utility Districts*, compiled by the Division of Municipal Audit. State statute requires

schools to follow the *Internal School Uniform Accounting Policy Manual*, compiled by the Tennessee Department of Education, the Department of Finance and Administration, and the Division of Municipal Audit. At the conclusion of an investigative audit, the division publishes a report which identifies internal control structure and compliance weaknesses and recommends corrective action. The audits point out to officials the importance of sound internal controls and compliance with applicable laws and regulations.

The division routinely provides technical assistance to local government officials and certified public accountants. This assistance often requires detailed research of financial accounting concepts and state and federal statutes.

Audits and Investigative Audits

For the year ended June 30, 2007, the Division of Municipal Audit performed 1.137 reviews of audit reports for specified local governments and other publicly funded entities. The division released 26 investigative audits during the year. The entities examined in the 26 investigative audits included 16 municipalities, 6 public schools, 2 nonprofit entities, 1 utility district and 1 housing authority. The majority of the investigative audits involved allegations of fraud, waste, and abuse. investigative audits revealed weaknesses in internal controls, absence of internal controls, or potential problem areas that created an environment conducive to fraud. During the 2007 fiscal year, investigative audits revealed losses of at least \$423,830 due to fraud. In total, over 17 defendants' cases were disposed of in fiscal year 2007. Eighty-eight counts were dealt with. In all, defendants were ordered to pay restitution of \$1,458.731.

Municipal Audit

The Division of Municipal Audit released the following investigative audit report during the year ended June 30, 2007:

Harpeth Middle School – Cheatham County Schools

Town of Alexandria

City of Clarksville - Mowing Services

City of Loudon

Lewisburg Housing Authority (w/DA letter)

Whitthorne Middle School - Maury County Schools

Hendersonville High School – Sumner County Schools

Jackson County Middle School – Jackson County Schools

Winchester Utilities

South East Tennessee Development District

New Johnsonville Fire Department

Red Boiling Springs School - Macon County Schools

Lexington Electric System

City of Lakewood

Loudon High School - Loudon County Schools

Citizens Gas Utility District

Spring Hill Police Department

City of Harriman

Lenoir City Utility Board

Memphis Intermodal Transfer Facility

Cumberland County Emergency and Rescue Squad

City of Manchester

City of Tullahoma

Town of Smyrna Police Department

City of Decherd Police Department

Gallaway Police Department



ince its inception, the hotline has received 11,756 calls, including 773 calls between July 1, 2006, and June 30, 2007. Of the 773 calls, 323 concerned allegations of fraud, waste, or abuse. The substantive calls—those relating to fraud, waste, or abuse—concerned a wide range of entities, including municipalities, counties, state agencies and departments, and federal agencies and departments. A more detailed analysis is below. Substantive calls are investigated by the Department of Audit or referred to the appropriate state agency or program.

Of the 323 calls referred for action, responses have been received on 285, and these are considered closed. The remaining 38 continue to be considered open.

The remaining 450 calls have not been acted on because they were either repeat calls or were not relevant to the purpose of the hotline. Calls in the latter group include wrong numbers, hang-ups, general inquiries about the hotline, and requests for service provided by other agencies, such as tax assistance. Where applicable, the callers are referred to the appropriate agency or department that can provide assistance.

Results of Hotline Calls

The following summaries are the results of hotline calls upon which corrective action was taken by the subject agency for the year ending June 30, 2007:

Human Services – Grantee Falsified Grant Proposal Documents

The caller alleged a grantee submitted false bid documentation as part of a grant administered by the department. The allegations were found to be true, and the grantee was required to repay \$13,300 to the department. The department canceled its contract with the grantee agency. The District Attorney's office declined to prosecute.

Human Services – Day Care Inappropriately Billed for Meals Not Served

The caller alleged that a daycare was not feeding children the meals it was receiving reimbursement for. The allegations were found to be true, and the department issued a Notice of Serious Deficiency to the daycare, and required it to enter into a corrective action plan. In addition, the department required the daycare to remit a check for \$2,874.75 for the overpayment.

Human Services – Failure to Reimburse Gas Bill Under Families First Program

The caller alleged that she had not received reimbursement for two months worth of gas bills under

the Families First program. The allegations were found to be true, and the caller received reimbursement.

Human Services - Child Support Arrearage

The caller alleged that the department was not properly processing the non-custodial parent's child support payments. The department determined that the non-custodial parent's employer was not properly assigning the payment. The department provided information to the employer regarding the wage assignment law.

Division of Mental Retardation Services – Illegal Parking in Handicap Parking Spaces

The caller alleged that a contracting agency's employees were illegally parking in handicapped spaces. The executive director issued a letter reminding all employees that they are not allowed to park in handicapped spaces unless issued a permit.

General Services – Excessive Phone Use by Housekeeping Staff

The caller alleged that members of the contracted housekeeping staff were making excessive personal telephone calls. Management created a new policy forbidding all employees, except supervisors, from bringing cell phones into the building.

Mental Health and Developmental Disabilities – Time and Attendance Abuse

The caller alleged that employees were falsely claiming time worked. Although the allegations could not be substantiated, the department moved to a centralized timekeeping process to provide additional safeguards against falsifying time records.

Transportation – Failure to Pick Up Service Recipient at Appointed Time

The caller alleged that a van driver failed to pick the caller up at a designated time. The allegation was confirmed. The service provider submitted a corrective action plan that requires a driver to inform the dispatcher if they are running late. In addition, the service provider installed new dispatching and scheduling software to assist the transportation program.

Health – Deficiency in Documentation of Client's Personal Items

The caller alleged that a drug and alcohol abuse center was fraudulently using the caller's food stamp card. Although the allegation could not be substantiated, the department did cite a deficiency in the center's documentation of client's moneys and/or valuables.

Health - Failure to Provide Hepatitis Shots

The caller alleged that she had been given a prescription for Hepatitis A and Hepatitis B shots, but the health department would not give her the shots. The allegations were substantiated and it was determined that the health department should have given the shots. The caller was contacted and offered the Hepatitis A shot and offered arrangements for the Hepatitis B shot.

Treasury – Personal Business on State Time

The caller alleged that an employee was conducting personal business on state time. The allegations were substantiated. The employee was suspended for five days without pay and forfeited six days of annual leave.

Division of Mental Retardation – Discrepancies in Documenting Personal Funds

The caller alleged that funds provided by the division to a service provider were not being properly utilized. The allegations could not be substantiated. However, the review disclosed discrepancies in the management of clients' personal funds and maintaining food stamp receipts adequately. The corrective plan required the service provider to reimburse \$6,063.99 to twenty-seven service recipients.

Comptroller - State Audit - Improper Internet Usage

The caller alleged that a state employee was making comments on Internet web sites during work hours. The allegation was substantiated. The employee resigned from the position.

Correction - Improper Computer Usage

The caller alleged that employees were playing computer games during work hours. Although the allegations could not be substantiated, all installed games were removed from the work computers.

Safety – Improper Actions by Employee and Inmate

The caller alleged that an employee took an inmate off a job site to a liquor store to purchase cigarettes and make personal phone calls. The allegation was substantiated. A written warning was issued to the employee. Counseling on Inmate Regulations while on work detail was recommended for the entire building staff and inmates.

Mental Health and Developmental Disabilities – Abusive Language and Behavior

The caller alleged that employees of a licensed agency used abusive language and behavior towards clients of the agency. Based on the investigation of the allegation a Notice of Non-Compliance was issued to the agency. Several deficiencies were noted in addition to the allegations in the complaint. Licensure staff returned and determined that corrections to the deficiencies were made.

Commerce and Insurance – Personal Business on State Time

The caller alleged that an employee was conducting personal business on state time. The allegations were substantiated. The employee received a written warning and was warned that future similar actions could result in termination.

County Audit - Questionable Tuition Expenses

The caller alleged that the county improperly paid for an employee's tuition to an alleged diploma mill. The allegation could not be substantiated. However, due to a lack of a countywide policy a finding was issued which recommended that the county adopt a policy that identifies what constitutes tuition and what limitations and accreditation requirements the county expects for colleges and universities.

Health - Client Neglect

The caller alleged that clients were being neglected, that the facility was understaffed, and the doctor in charge was not qualified. Allegations regarding staffing and the qualifications of the doctor were unsubstantiated. The facility was cited with deficiencies in its condition and a plan of correction was submitted.

Agriculture - Services Offered Free of Charge

The caller alleged that an employee was providing a department service free of charge when there was a cost associated with the service. The allegation could not be substantiated. However, the department issued a department wide memorandum reminding employees that any source of revenue should never be provided free of charge.

Agriculture - Simultaneous Employment

The caller alleged that an employee was working another job while on state time. The allegation was substantiated. The department recommended that the employee be terminated. As a result of the employee's due process hearing, the recommended disciplinary charges were reduced to a 30 day without pay suspension and the repayment of 34.6 hours equaling \$496.06. This decision is under appeal.

County Audit - Paving Non-County Road

The caller alleged that the County Highway Department paved an individual's driveway. The paved area does not appear to be on the county's road list. A finding will be included in the county's report unless other documentation can be provided to show the paved area as a county road.

Transportation – Personal Errands on State Time

The caller alleged that an employee was doing personal errands on state time and not taking leave for that time. The allegation was substantiated. The employee resigned in lieu of termination.

County Audit – Misuse of County Property and Employee Time Abuse

The caller alleged that employees were clocking in and then going to breakfast, that a Highway Department tractor was kept at an employees house when not in use, and that the Highway Department used equipment belonging to an employee. Findings and recommendations were included in the county's audit report.

Tennessee Board of Regents – State Employees for Personal Use

The caller alleged that an employee was using other employees to do personal work while on state time. The allegation was substantiated. The employee resigned from the position. The Board is seeking repayment of \$7,783.82 from the employee.

Comptroller's Fraud, Waste and Abuse Hotline (800) 232-5454

Analysis of Substantive Hotline Calls Fiscal Year Ended June 30, 2007

Agency Involved	# of Calls	# Responded	# Outstanding
Local Government			
	23	22	1
Municipal Audit City of Clarksville	1	1	0
Metro Nashville	2	2	ő
			ŭ
County Government	24	22	2
County Audit	24	22	2
State Government	_	4	
Administrative Office of the Courts	1	1	0
Department of Agriculture	2	2	0
Board of Probation and Parole	2	2	0
Board of Regents	10	1	9
Department of Children's Services	23	22	1
Department of Commerce and Insurance	1	1	0
Commission on Aging	4	2	2
Comptroller-State Audit	2 2	1	1 0
Comptroller-Property Assessments	1	2 1	0
Department of Correction	6	3	3
Division of Mental Retardation	3	2	1
Department of Education	5	5	0
Department of Environment and Conservation	4	1	3
Department of Finance and Administration	4	4	0
Department of General Services	32	32	0
Department of Health	42	41	1
Department of Human Services	3	2	1
Department of Labor and Workforce Develop.	20	17	3
Department of Mental Health and Dev. Dis.	5	5	0
Department of Revenue	62	58	4
Department of Safety Bureau of TennCare	3	3	0
Tennessee Student Assistance Corporation	2	2	0
Tennessee Wildlife Resources Agency	1	1	0
Department of Transportation	21	20	1
Department of Transportation Department of the Treasury	1	1	0
University of Tennessee	1	1	0
Federal Government			
	3	2	1
Head Start	1	0	1
Legal Services Corporation	3	0	3
Social Security	5	0	5
<u>Miscellaneous</u>	_		
Salvation Army	3	3	0
Total	323	285	38



he department's professional staff perform a wide variety of audit work requiring different types of training and experience. Therefore, members of the staff have degrees in fields such as accounting, public administration, information systems, law, political science, criminal justice, education, and nursing. More than 60 of the professional staff have advanced degrees. The department encourages its employees to pursue professional certifications such as Certified Public Accountant, Certified Information Systems Auditor, Certified Fraud Examiner, and Certified Government Financial Manager.

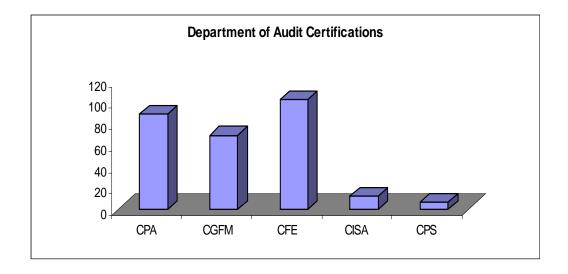
Professional Development

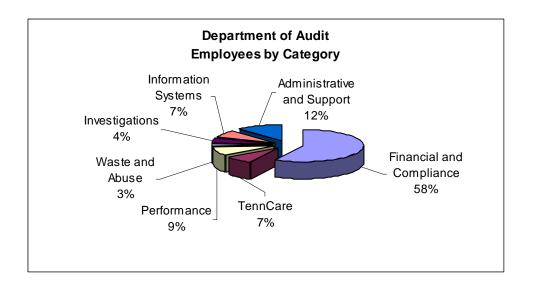
As of June 30, 2006, 178 employees of the department had received one or more professional certifications. This range of experience gives a broad perspective to the department's audit work.

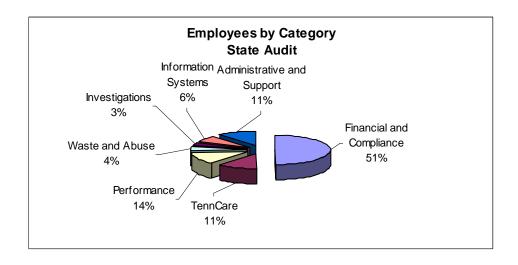
The Department of Audit ensures its auditors receive the required continuing professional education to meet certification standards and *Government Auditing Standards*. Auditors participate in the department's in-house training

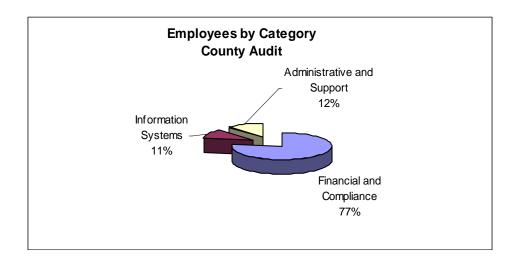
program as course developers, presenters, and participants. Over 18,966 hours of training were completed during the fiscal year ended June 30, 2007.

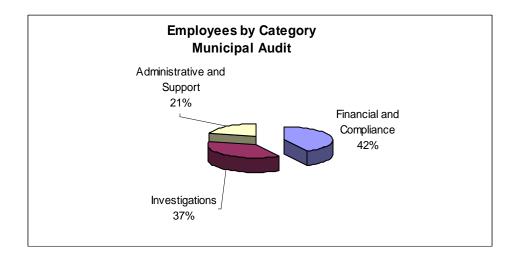
The Department of Audit fully supports its staff's active participation in local professional organizations, recognizing that these organizations contribute to the staff's continued growth.

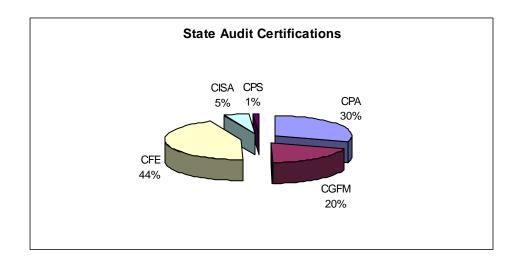


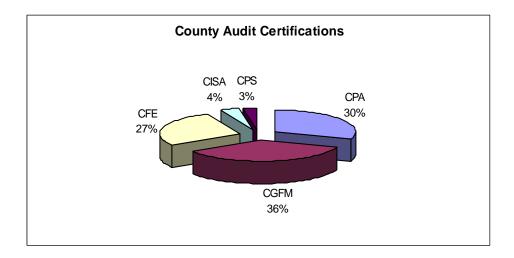


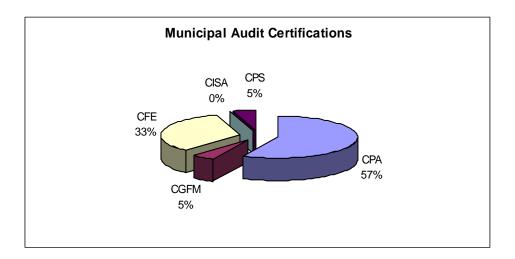






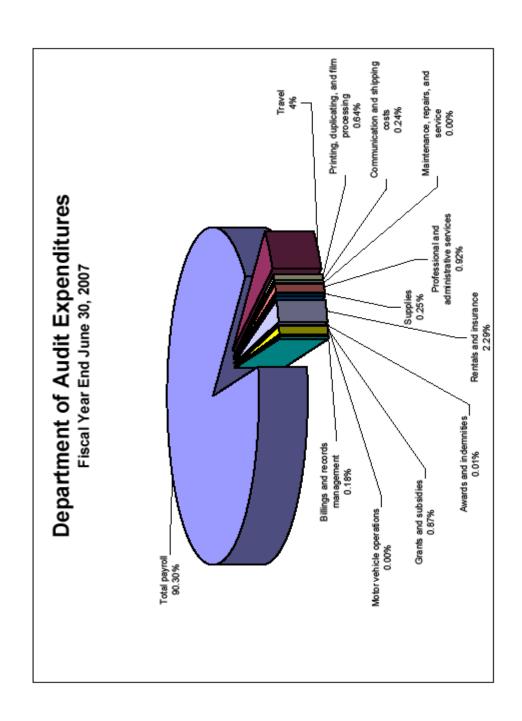




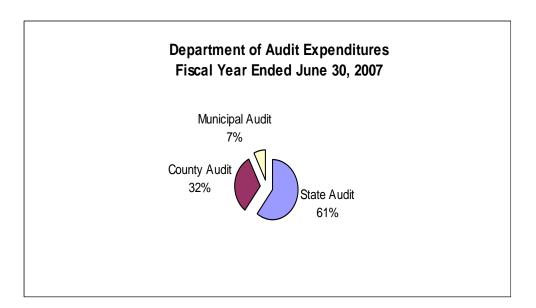




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Financial Information





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Comptroller's Fraud, Waste and Abuse Hotline (800) 232-5454

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